

Report
of the
Examination of
North Central Health Protection Plan
Wausau, Wisconsin
As of December 31, 1998

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October 21, 1999

Honorable Connie L. O'Connell
Commissioner of Insurance
Madison, Wisconsin

Commissioner:

In accordance with your instructions, a compliance examination has been made of
the affairs and financial condition of:

NORTH CENTRAL HEALTH PROTECTION PLAN
Wausau, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of North Central Health Protection Plan (NCHPP or the HMO) was conducted in 1996 as of December 31, 1995. The current examination covered the intervening period ending December 31, 1998, and included a review of such 1999 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the HMO's operations, and included the following areas:

- History
- Management and Control
- Corporate Records
- Conflict of Interest
- Fidelity Bonds and Other Insurance
- Provider Contracts
- Territory and Plan of Operations
- Affiliated Companies
- Growth of the HMO
- Reinsurance
- Financial Statements
- Accounts and Records
- Data Processing
- Enrollee Complaint Procedure
- Underwriting

Emphasis was placed on the audit of those areas of the HMO's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the HMO to satisfy the recommendations and comments made in the previous examination report.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the HMO's operations is contained in the examination work papers.

The HMO is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

II. HISTORY AND PLAN OF OPERATION

NCHPP can be described as a nonprofit, network model health maintenance organization (HMO) insurer. An HMO insurer is defined by s. 609.01 (2), Wis. Stat., as "... a health care plan offered by an organization established under ch. 185, 611, 613, or 614 or issued a certificate of authority under ch. 618 that makes available to its enrolled participants, in consideration for predetermined fixed payments, comprehensive health care services performed by providers selected by the organization." Under the network model, the HMO provides care through contracts with clinics and otherwise independent physicians operating out of their separate offices. HMOs compete with traditional fee-for-service health care delivery.

The HMO was incorporated as a health care cooperative under ch. 185, Wis. Stat., on November 18, 1980, and commenced business December 1, 1980. The membership classes of NCHPP are described under the caption "Board of Directors" in the Management and Control section of this report.

According to its business plan, the HMO's service area is comprised of the following counties:

Forest	Lincoln	Oneida	Price	Vilas
Langlade	Marathon	Portage	Taylor	Wood

NCHPP, as a network model, contracts with individual physicians and clinics for the provision of health care services to plan enrollees. The plan is divided between two regions, the Standard Core region and the Northern region. The plan reimburses participating physicians on a fee-for-service basis. NCHPP submits a fee schedule to providers at January 1 of each year. Each new plan year the board approves an across-the-board percentage increase to the fee schedule. NCHPP provides primary and specialty care service through 450 participating physicians and 1,226 specialist physicians.

Physicians in the Core Region are reimbursed at 94% of NCHPP fee-for-service charges, with 6% withheld and placed into a withhold pool. Physicians in the Northern Region are reimbursed at 90% of NCHPP's fee schedule. Physicians' fees in excess of \$200,000 per enrollee per year are covered by NCHPP. As noted in the section of this report captioned

“Reinsurance and Corporate Insurance,” NCHPP has a stop-loss reinsurance policy which covers claims in excess of \$200,000 per enrollee per plan year.

The physicians’ agreement provides for a distribution to the providers of the withheld amount at year-end, dependent on NCHPP’s results for the year. The distribution to the individual physicians is based on a formula that is designed to reward cost-efficient providers and penalize overutilizing physicians. The agreement provides that the responsibility of the physicians to cover deficits is limited to the 6% withhold.

The term of provider participation contracts is from January 1 to December 31 (known as the “plan year”) and continue in force and effect until canceled. Cancellation of the agreement may be made by either party upon 30 days’ prior written notice, effective as of the end of any plan year.

The agreements require the provider to maintain liability insurance in compliance with ch. 655, Wis. Stat. The agreements contain adequate hold-harmless clauses in which the provider “agrees that under no circumstance will the provider seek any compensation for services from enrollees except for deductibles, amounts otherwise payable by other plans and insurers or copayments, if any, and noncovered services.”

NCHPP’s policy allows enrollees free choice of any licensed physician who agrees to participate in the plan. Referrals need the authorization of the plan’s medical director. Enrollees have access to emergency rooms at contracted and affiliated hospitals on a 24-hour basis.

Major provider systems contracting with NCHPP include the Marshfield Clinic, Preferred Health Services [which includes Wausau Hospital & Wausau Regional Healthcare], and members of Ministry Health Care. The HMO has also contracted with Covenant Healthcare System, Inc. (d/b/a Covenant Behavioral Health Services) to act as a manager of the delivery of mental health services to NCHPP enrollees. Covenant is compensated on a capitation basis.

The HMO currently contracts with 17 hospitals to provide inpatient and outpatient services. Contracting hospitals are generally paid on a fee-for-service or per-diem rate basis with a 6% withhold from each claim or charge paid during the plan year. The withhold may be distributed to the hospital or retained to offset a deficit in the medical fund. Several hospitals are

paid on a discounted fee-for-service schedule. The contracts include hold-harmless provisions for the protection of policyholders. The contracting hospitals are as follow:

Day Surgery Plus	Riverview Hospital
Eagle River Memorial Hospital	Sacred Heart Hospital
Flambeau Hospital Inc.	St. Joseph's Hospital, Marshfield, Wisconsin
Good Samaritan Health Center	St. Mary's Hospital
HealthSouth Surgery Center of Wausau	St. Michael's Hospital
Howard Young Medical Center	Wausau Hospital Center
Langlade County Memorial Hospital	Wausau Kidney Center
Memorial Hospital of Taylor County, Inc.	Wausau Kidney Center/Rice Clinic
North Central Health Care Facilities	

The following is a listing of contracted hospitals in which a member is required to obtain a referral for admission:

- Abbott Northwestern Hospital
- Children's Hospital of Wisconsin
- Horizon Health Care
- Medical College of Wisconsin
- St. Luke's Heart Plan, S.C.
- St. Luke's Medical Center Inc.
- United Resource Network
- University of Wisconsin Hospital and Clinics

NCHPP offers comprehensive health care coverage which may be changed by riders to include deductibles, coinsurance, and copayments. The following basic health care coverages are provided:

- Physician services
- Inpatient services
- Outpatient services
- Mental health, drug, and alcohol abuse services
- Ambulance services
- Special dental procedures (oral surgery, TMJ)
- Prosthetic devices and durable medical equipment
- Newborn services
- Home health care
- Preventive health services
- Diabetes treatment
- Routine eye examinations
- Extended care facility services—typically limited to 30 days
- Prescription drugs
- Cardiac rehabilitation, physical, speech, and/or occupational therapy
- Kidney disease treatment
- Certain transplants
- Chiropractic services

Plan coverage is contingent on nonemergency services being provided by participating physicians and hospitals or on the referral of participating physicians. Inpatient

mental health and AODA coverage is limited to 20 days; outpatient mental health and AODA coverage is limited to 30 visits per year. Beginning January 1, 1998, Covenant began to preauthorize behavioral health services.

NCHPP also offers point-of-service (POS) and point-of-enrollment plans. NCHPP calls its point-of-enrollment plan Prime Care.

Under POS, the enrollee can choose to receive care from a participating or nonparticipating provider. An individual selecting a nonparticipating provider incurs higher levels of out-of-pocket costs and reduced levels of covered benefits.

Under Prime Care the enrollee must choose a primary care physician (PCP) from the list of participating providers. Specialty care can only be received through a referral from a PCP. The referring PCP does not have to be the PCP chosen at the time of enrollment. Referrals are not required for the following specialty care: chiropractic care, behavioral health, eye exams, and chronic renal failure/dialysis services.

The HMO also provides administrative services (ASO) to groups which choose to self-insure. The self-insured groups pay NCHPP a monthly service fee per each employee in the self-insured group's medical plan. The self-insured groups purchase and maintain stop-loss insurance. The ASO contracts include withhold provisions, with payment dependent on the plan's experience for the year, similar to those for insured business.

The HMO currently markets to groups and individuals. Small employer groups, of up to 25 employees, are written through a trust arrangement. Marketing staff is provided by EMPLOYERS INSURANCE OF WAUSAU A Mutual Company (EIW), under an administrative services agreement, as is further discussed in the Management and Control section of this report.

The HMO uses an actuarially determined base as a beginning point in premium determination. This rate is adjusted for age/gender distribution, benefit plan, area, trend, and administrative cost on a group-by-group basis. Experience is reviewed for renewal groups; credibility factors are used to blend the "book" rate with the experience rate, giving more weight to the experience portion of the rate as the group size increases. Small groups are handled

separately, using a rate tier system to recognize medical risk factors within the requirements set forth by the state.

The HMO has developed procedures to monitor the actions of its healthcare providers. NCHPP has a Quality Management Program which focuses on improving the availability, accessibility, appropriateness, and effectiveness of the healthcare provided to plan members. The program is directed by the medical quality management committee, which reports to the medical director. Supporting task force committees include credentialing, utilization management, and chiropractic peer review; as well as the pharmacy and therapeutic committee of Wausau Insurance Companies. As another control feature, all elective out-of-plan referral procedures and select outpatient tests and procedures must be preauthorized by the HMO's medical director. For each inpatient stay not preauthorized, covered expenses will be reduced by a specified amount (\$200-500, varies by contract).

NCHPP has in place a grievance procedure pursuant to s. Ins 3.50 (10), Wis. Adm. Code. The grievance procedure is explained in the plan member's certificate of coverage.

III. MANAGEMENT AND CONTROL

Board of Directors

The board of directors consists of ten members. Directors are elected annually to serve a one-year term. Three directors represent policyholders [Class A members]. Two members are designated by Community Health Care, Inc. (CHC) [Class B members]. Wausau Insurance Companies (WIC) or any subsidiaries or affiliates thereof, are given the authority to appoint two directors, representing the HMO administrator [Class C members]. Class D members consist of the HMO's providers and designate two directors, one representing providers of Wausau Regional Health Care, Inc. (WRHC) and one representing non-WRHC providers in Marathon county. Finally, the president of NCHPP serves as a director [Class E member]. Officers are appointed by the board of directors. The board members currently receive a \$100 monthly retainer and \$200 for each monthly meeting attended for serving on the board. In months where more than one board meeting is held, members receive \$300 for each extra meeting. Executive committee members receive \$100 for each committee meeting attended.

Currently the board of directors consists of the persons listed at the top of the next page. The letter after each individual's name indicates which membership class the director represents.

Name and Residence		Principal Occupation	Term Expires
James P. Binder, MD Wausau, WI	(D)	Physician, Surgical Associates, SC	2000
Dwight D. Davis Wausau, WI	(C)	CEO, Wausau Insurance Companies	2000
Eugene S. Lohr Wisconsin Rapids, WI	(A)	Manager—Product & Process Improvement, Georgia-Pacific	2000
Michael L. McDonald Mosinee, WI	(A)	Senior Vice President—Administration, Wausau-Mosinee Papers	2000
Alfred P. Moore Wausau, WI	(C)	Senior Vice President, Wausau Insurance Companies	2000
Charles L. Shabino, MD Wausau, WI	(B)	Chief Medical Officer, Community Health Care	2000
Paul A. Spaude Wausau, WI	(B)	Chief Administrative Officer, Community Health Care	2000
David B. Tange, MD Mosinee, WI	(D)	Physician, Kronenwetter Clinic	2000
Robert A. Wagman Schofield, WI	(A)	President, Wausau Carriers	2000
Jeffrey L. Zriny Wausau, WI	(E)	President & CEO, NCHPP	2000

Officers of the Company

The officers elected or appointed by the board of directors and serving at the time of this examination are as listed below. Officers are compensated by EMPLOYERS INSURANCE OF WAUSAU A Mutual Company.

Name	Office
Robert A. Wagman	Chairperson
Jeffrey L. Zriny	President
Eugene S. Lohr	Vice President
Alfred P. Moore	Asst. Vice President
John L. Baker	Secretary/Treasurer
James P. Binder, MD	Asst. Treasurer
Paul A. Spaude	Asst. Secretary

Committees of the Board

The HMO's bylaws allow for the formation of certain committees by the board of directors. At the time of the examination, the HMO had an executive committee consisting of the following members:

Executive Committee

Jeffrey Zriny, Chair
Robert Wagman
Alfred Moore
Paul Spaude
James Binder

In addition, NCHPP has the following management committees, which report to the board:

Finance Committee
Marketing Committee
Utilization Management Committee
Medical Quality Management Committee
Credentialing Committee

Contractholder Advisory Committee
Physician Advisory Committee
Northern Region Operating Committee
Chiropractic Peer Review Committee

The HMO has no employees. Necessary staff is provided through an administrative services agreement with EMPLOYERS INSURANCE OF WAUSAU A Mutual Company (EIW). Under the agreement, effective January 1, 1997, EIW's duties include marketing, underwriting, contract issuance, premium billing and collection, claims administration, actuarial services, maintenance of accounting and other records, and provision of data systems. EIW's general administration fee is based on a per-enrollee-per-month amount, with the agreement setting forth additional fees for individual conversion policies and the HMO's 65-Plus product. Under an amendment to the contract effective in 1999, NCHPP agrees that EIW will receive a minimum of \$530,000 per month. Four percent of the administrative fee is withheld. The withhold is paid if the HMO has distributable surplus at the end of the year. In addition, the 1999 amendment to the contract established a number of performance standards for EIW. For each standard not met, EIW is required to give NCHPP a credit of 0.25% of the fee for the period, up to an aggregate annual maximum credit of 5%. The initial term of the agreement is through December 31, 2002, automatically renewing for additional three-year terms thereafter, unless otherwise terminated. The agreement may be terminated under the following circumstances: by OCI, with 30 days'

written notice, to protect the interest of NCHPP's members, enrollees, or creditors, or the public; automatically should NCHPP not be able to legally continue operations; automatically upon bankruptcy of either party; upon 30 days' written notice by either party if default of an obligation continues 60 days after notice of such default; or by NCHPP with 60 days' prior written notice, in the event EIW lacks the capability to provide substantially all the services under the agreement within the HMO's service area.

Financial Requirements

The financial requirements for an HMO under s. Ins 3.50, Wis. Adm. Code, are as follows:

	Amount Required
1. Minimum capital or permanent surplus	Either: \$750,000, if organized on or after July 1, 1989 or \$200,000, if organized prior to July 1, 1989
2. Compulsory surplus	The greater of \$750,000 or: If the percentage of covered liabilities to total liabilities is less than 90%, 6% of the premium earned in the previous 12 months; If the percentage of covered liabilities to total liabilities is at least 90%, 3% of the premium earned in the previous 12 months
3. Security surplus	The greater of: 140% of compulsory surplus reduced by 1% of compulsory surplus for each \$33 million of additional premiums earned in excess of \$10 million or 110% of compulsory surplus
4. Operating funds	Funds sufficient to finance any operating deficits in the business and to prevent impairment of the insurer's initial capital or permanent surplus or its compulsory surplus

Covered liabilities are those due to providers who are subject to statutory hold-harmless provisions.

In addition, there is a special deposit requirement equal to the lesser of the following:

1. An amount necessary to maintain a deposit equaling 1% of premium written in this state in the preceding calendar year;
2. One-third of 1% of premium written in this state in the preceding calendar year.

The HMO has satisfied this requirement for 1998 with a deposit of \$723,000 with the State Treasurer. See further comment in the section of this report captioned Summary of Current Examination Results.

Insolvency Protection for Policyholders

Under s. Ins 3.50, Wis. Adm. Code, HMOs are required to provide continuation of coverage for its enrollees. These requirements are the following:

1. Enrollees hospitalized on the date of insolvency will be covered until discharged; and
2. Enrollees will be entitled to similar, alternate coverage which does not contain any medical underwriting or preexisting limitation requirements.

The HMO has met this requirement through its reinsurance contract, as discussed in the Reinsurance section of this report.

IV. REINSURANCE AND CORPORATE INSURANCE

The HMO has reinsurance coverage under the contract outlined below:

Reinsurer:	EMPLOYERS INSURANCE OF WAUSAU A Mutual Company
Type:	Individual Stop Loss
Effective date:	January 1, 1998; renews every January 1
Retention:	\$200,000
Coverage:	The amounts paid for any one person in any one policy year under a group medical benefits contract that exceeds the deductible.
Premium:	<p>\$2.10 per enrollee per month</p> <p>The contract includes provision for an annual calculation of a premium stabilization fund. A "Gross Available Fund Amount" is calculated based on a number of factors, including premium earned by the HMO, coverage payments made by the reinsurer, and risk charge and interest factors.</p> <p>If the resulting fund amount is greater than or equal to zero, the HMO receives a refund equal to the greater of (1) the remainder determined by subtracting premium from the gross available fund amount or (2) 20% of the gross available fund amount. The remaining fund amount is carried forward into the next year's calculation as the Premium Stabilization Fund.</p> <p>If the resulting amount is negative, no refund is made. The lesser of the fund amount or -50% of premium is carried into the next year's calculation as the Premium Stabilization Fund.</p>
Termination:	By the HMO giving 60 days' written notice prior to the expiration of a term; by the reinsurer giving not less than 10 days' written notice for nonpayment of premium, material misrepresentation, substantial change in risk assumed, or substantial breaches of contractual duties.

The reinsurance policy contains the following insolvency provisions:

1. Reinsurer will continue plan benefits for enrollees who are confined in an acute-care hospital on the date of insolvency until their discharge.
2. Reinsurer will make available to all enrollees similar alternate coverage which does not contain any medical underwriting or preexisting limitation requirements.

In addition, the HMO is provided with corporate insurance coverage under the contracts listed below:

Type of Coverage	Policy Limits
Directors' and officers' liability	\$5,000,000
Managed care organization liability (professional liability and errors & omission)	5,000,000

The above coverages were obtained through TIG Specialty Insurance Company, which is on the Commissioner's current list of approved surplus lines insurers.

V. FINANCIAL DATA

The following financial statements reflect the financial condition of the HMO as reported in the December 31, 1998, annual statement to the Commissioner of Insurance. The current examination did not result in any adjustments to surplus. Also included in this section are schedules that reflect the growth of the HMO for the period under examination.

**North Central Health Protection Plan
Balance Sheet
As of December 31, 1998**

Current Assets:

Cash and cash equivalents	\$(1,705,951)	
Short-term investments	7,230,000	
Premiums receivable--net	508,973	
Investment income receivable	114,446	
Reinsurance recoverable on paid losses	101,426	
DPS/ProVantage receivables	258,504	
ASO receivables	298,323	
POS receivables	57,755	
Other receivables	11,140	
Accounts receivable – administrative service fee	<u>76,078</u>	
Total current assets		\$ 6,950,694

Other Assets:

Bonds	<u>9,737,634</u>	
Total other assets		<u>9,737,634</u>

Total Assets		<u>\$16,688,328</u>
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Current Liabilities:

Accounts payable	\$ 21,412	
Claims payable (reported and unreported)	7,779,754	
Accrued medical incentive pool	314,624	
Unearned premiums	682,007	
Miscellaneous liabilities	224,007	
Active life reserve	130,000	
ASO withhold	803,838	
Loss expense reserves	<u>153,195</u>	
Total current liabilities		\$10,108,837

Other Liabilities:

Advance deposit	<u>136,226</u>	
Total other liabilities		<u>136,226</u>

Total Liabilities		10,245,063
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Net Worth:

Surplus notes	2,000,000	
Retained earnings/fund balance	<u>4,443,265</u>	
Total net worth		<u>6,443,265</u>

Total Liabilities and Net Worth		<u>\$16,688,328</u>
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**North Central Health Protection Plan
Statement of Revenue and Expenses
For the Year 1998**

Revenues

Premium	\$68,273,030	
Investment	<u>972,371</u>	
Total revenue		<u>\$67,245,401</u>

Medical and Hospital Expenses

Physician services	27,497,131
Other professional services	9,752,625
Outside referrals	1,513,952
Emergency room, out-of-area	13,036,788
Inpatient	11,761,234
Incentive pool and withhold adjustments	(2,053,021)
Active life reserve	<u>40,000</u>
Subtotal	61,548,709

Less:

Net reinsurance recoveries incurred	(160,362)	
COB and subrogation	<u>650,914</u>	
Subtotal		
Total medical and hospital		61,058,157

Administrative Expenses

Total administrative expenses	<u>5,377,684</u>
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Total expenses	<u>66,435,841</u>
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Net Income/(Loss)	<u>\$ 809,560</u>
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**Statement of Net Worth
As of December 31, 1998**

Net worth, beginning of year	\$5,821,454
Increase (decrease) in retained earnings/fund balance:	
Net income (loss)	809,560
Interest on surplus notes	(168,740)
Decrease (increase) in nonadmitted assets	<u>(19,009)</u>
Net worth, end of year	<u>\$6,443,265</u>

**North Central Health Protection Plan
Statement of Cash Flows (Indirect Method)
As of December 31, 1998**

Cash Flows From Operating Activities

Net income (loss)	\$ 809,560
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:	
Depreciation and amortization	146,565
Change in operating assets and liabilities	
(Increase)/decrease in operating assets:	
Premium receivable	286,213
Write-ins for (increase)/decrease in operating assets:	
Miscellaneous receivable	166,636
Reinsurance recoverable on paid losses	2,673,858
Increase/(decrease) in operating liabilities:	
Medical claims payable	(1,830,246)
Unearned premiums	529,251
Accounts payable	(106,503)
Accrued medical incentive pool	74,682
Write-ins for (increase)/decrease in operating liabilities:	
Miscellaneous liabilities	<u>315,246</u>
Net cash provided from (used by) operating activities	\$ 3,065,262

Cash Flows From Investing Activities

Receipts from investments	\$ 3,321,243
Payments for investments	(7,478,648)
Write-ins for investing activities:	
Accrued interest	<u>54,723</u>
Net cash provided from (used by) investing activities	(4,102,682)

Cash Flows From Financing Activities

Write-ins for financing activities:	
Interest on surplus notes	<u>(168,740)</u>
Net cash provided from (used by) financing activities	<u>(168,740)</u>

Net increase (decrease) in cash and cash equivalents	(1,206,160)
Cash and cash equivalents at beginning of year	<u>(499,791)</u>
Cash and cash equivalents at end of year	<u><u>\$ (1,705,951)</u></u>

Growth of North Central Health Protection Plan

Year	Assets	Liabilities	Net Worth	Premium & Related Revenue	Medical Expenses Incurred	Net Income
1998	\$16,688,328	\$10,245,063	\$6,443,265	\$66,273,030	\$61,058,157	\$ 809,560
1997	17,084,087	11,262,633	5,821,454	69,829,294	64,599,644	(750,000)
1996	14,841,579	10,139,138	4,702,441	70,521,959	67,317,395	(750,000)
1995	13,630,165	8,177,724	5,452,441	61,662,259	58,092,891	(360,836)

Enrollment and Utilization

Year	Enrollment	Hospital Days/1,000	Average Length of Stay
1998	38,398	263.79	3.4
1997	46,900	235.61	3.6
1996	47,213	276.08	3.8
1995	40,969	261.00	3.5

Assets have increased 22% since the previous examination, but declined 2% between 1997 and 1998. Net worth has varied during the last three years; overall showing an increase of 18% from 1995 to 1998.

The HMO reported net income in 1998 for the first time in recent years. Prior to 1998, NCHPP had an aggregate stop-loss coverage arrangement with EIW, which covered losses over \$750,000.

While enrollment is little changed from 1995, it has decreased 18.7% from a high of 47,213 in 1996 to the 1998 level.

Per Member Per Month Information

The following table is calculated from data in NCHPP's filed statutory annual statement:

	1998	1997	Percentage Change
Premiums:	<u>\$140.58</u>	<u>\$127.73</u>	10.06%
Expenses:			
Physicians services	58.33	61.43	-5.05
Other professional services	20.69	19.73	4.87
Outside referrals	3.21	2.45	31.02
Emergency room and out-of-area	27.65	26.18	5.61
Inpatient	24.95	23.20	7.54
Incentive pool & withhold adjustments			
Other medical & hospital	0.08	0.00	---
Reinsurance recoveries incurred	0.34	(5.53)	-106.15
COB and subrogation	<u>(1.38)</u>	<u>(2.33)</u>	-40.77
Total Medical	129.52	118.16	9.61
Administrative Expense	<u>11.41</u>	<u>12.54</u>	-9.01
Total Expenses	<u>\$140.93</u>	<u>\$130.70</u>	7.83%

The following table is compiled from NCHPP's internal PMPM summary. For its internal management report, the HMO includes both insured and ASO-business as "members."

	1998	1997	Percentage Change
Premiums:	<u>\$142.92</u>	<u>\$130.59</u>	9.44%
Capitation & Benefits Incurred	131.85	126.47	4.25
Direct Expenses	1.35	1.70	-20.59
Administrative Expenses	<u>10.67</u>	<u>10.22</u>	4.40
Total Expenses	<u>\$143.87</u>	<u>\$138.39</u>	3.96%

VI. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were three specific financial comments and recommendations in the previous examination report. The prior report also contained 16 market regulation comments and recommendations. Concurrent with this examination, the bureau of market regulation was expected to examine the company and its compliance with the prior market conduct recommendations. The financial comments and recommendations contained in the last examination report and actions taken by the HMO are as follows:

1. Investments—It is again recommended that the cooperative update its custodial safekeeping agreement to provide necessary safeguards as outlined in the NAIC Examiners Handbook.

Action—Noncompliance, see comments in the summary of current examination results.

2. Conflict of Interest—It is recommended that the cooperative obtain conflict of interest statements from its directors and officers on an annual basis.

Action—Compliance.

3. Supplemental Filing—It is recommended that the cooperative split its enrollment between HMO and POS on future filings of the HMO Enrollment By Service Area.

Action—Compliance.

Summary of Current Examination Results

Management and Control

As discussed earlier in this report, EIW provides staff and services to NCHPP under an administrative services agreement. Examination review indicated that the agreement was most recently amended effective January 1, 1999. The amendment, signed in May 1999, created or altered nine exhibits to the agreement. While some of the changes were minor, others were more significant, as modifications were made to the fee mechanism of the agreement and new categories of performance and service standards were created. Pursuant to s. 611.67 (3), Wis. Stat., HMOs are required to file management contracts with the Commissioner. The Commissioner has the opportunity to disapprove them. In addition, under s. Ins 3.50 (6), Wis. Adm. Code, these amendments are considered substantial changes in business plan, which is defined to include changes in plan administration. It is recommended that the HMO file all material changes in its administrative services agreement with OCI, as required by s. 611.67, Wis. Stat., and s. Ins 3.50 (6), Wis. Adm. Code.

Investments

A review of the custodial agreement indicated the agreement does not meet the standards of the NAIC *Financial Condition Examiners Handbook* model for custodial or safekeeping agreements. The Handbook sets forth the following suggested language for custodial agreements:

"shall contain satisfactory safeguards and controls, including but not limited to provisions requiring:

1. That the bank or trust company as custodian is obligated to indemnify the insurance company for any loss of securities of the insurance company in the bank or trust company's custody occasioned by the negligence or dishonesty of the bank or trust company's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction;
2. That in the event that there is a loss of the securities for which the bank or trust company is obligated to indemnify the insurance company, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced."

While the agreement has been changed since the previous examination, it still does not contain all of the NAIC suggested language. The agreement did not mention prompt replacement of

securities to the HMO, as required by point 2. It is again recommended that the HMO update its custodial agreement to provide for the necessary safeguards as outlined in the NAIC *Financial Condition Examiners Handbook*.

As noted earlier in this report under the heading “Financial Requirements,” the HMO is required to maintain a special deposit under s. 609.98, Wis. Stat. Examination review indicated that \$310,000 of this deposit was a security that matured on May 15, 1999. Records indicated that action was not taken to replenish this balance and request release of the matured security until October 1, 1999. This lack of timely action denied the HMO the opportunity to earn investment income. It is recommended that the HMO require its management company to establish a procedure so that securities are replenished in a timely manner.

Annual Statement

According to the NAIC *Annual Statement Instructions—HMO*, percentage withholds from providers are to be included in the Claims Payable line. The line for Accrued Medical Incentive Pool is to include the “liability for arrangements whereby the HMO agrees to share utilization savings with...providers”, but exclude percentage withhold arrangements. Review of the HMO’s accounts reported as Accrued Medical Incentive Pool indicated that the majority pertained to percentage withhold arrangements with providers. As the dollar total for these accounts fell below materiality considerations for this examination, a reclassification of balances is not being made. It is recommended that the HMO properly report amounts withheld under provider contracts as part of Claims Payable in future statutory financial statements, as required by the NAIC *Annual Statement Instructions—HMO*.

Disaster Recovery Plan

The HMO’s operations are performed by employees of EIW pursuant to an administrative services agreement. In addition to the employees and facilities, the HMO’s operations are administered on software developed by EIW. An indemnification clause within the agreement provides NCHPP protection from the negligence of EIW, unless it was under the direction or instruction of the HMO.

EIW personnel indicated that the HMO would rely on the disaster recovery/contingency planning of EIW in the event of a disaster. The administrative services agreement does not specifically address disaster recovery/contingency planning issues. In addition, a review of the board minutes did not evidence that disaster recovery/contingency plans were addressed at that level.

Disaster recovery/contingency plans are usually created and maintained by a company or one of its affiliates, and not a third party service provider. Since the administrative services agreement does not explicitly address this issue, it is recommended that the board formally acknowledge and document its acceptance of EIW's disaster recovery/contingency plans.

Compulsory Surplus Requirement

As noted in the section of this report captioned "Financial Requirements," HMOs are required to maintain minimum compulsory surplus. The HMO's calculation as of December 31, 1998, as modified for examination adjustments is as follows:

Assets		\$16,688,328	
Less:			
Special deposit		727,947	
Liabilities		10,245,063	
Examination adjustments		<u>0</u>	
Total			\$5,715,318
Net premium earned—HMO	\$66,088,089		
Compulsory factor	<u>3%</u>	1,982,643	
Net premium earned—Incidental Indemnity	184,942		
Compulsory factor	<u>10%</u>	<u>18,494</u>	
Compulsory surplus			<u>2,001,137</u>
Compulsory excess			<u>\$3,714,181</u>

VII. CONCLUSION

North Central Health Protection Plan is a nonprofit, network model HMO, organized as a cooperative. The HMO has been in operation for the past 18 years, in ten counties in central and northern Wisconsin. NCHPP contracts with EMPLOYERS INSURANCE OF WAUSAU for administrative services.

The HMO has had mixed results during the examination period. Net worth has increased 18% since 1995 and assets have increased 22%; total assets declined 2% between 1997 and 1998. In 1998, NCHPP reported net income for the first time in recent years, in the amount of \$809,560. In its most recent quarterly statement for 1999, the HMO reported a net loss of (\$1,700,229).

The examination found the HMO to be in compliance with two out of three prior examination recommendations. The current examination resulted in five recommendations, as summarized on the next page, and no adjustments to surplus.

VIII. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 23 - Management and Control—It is recommended that the HMO file all material changes in its administrative services agreement with OCI, as required by s. 611.67, Wis. Stat., and s. Ins 3.50 (6), Wis. Adm. Code.
2. Page 24 - Investments—It is again recommended that the HMO update its custodial agreement to provide for the necessary safeguards as outlined in the NAIC *Financial Condition Examiners Handbook*.
3. Page 24 - Investments—It is recommended that the HMO require its management company to establish a procedure so that securities are replenished in a timely manner.
4. Page 24 - Annual Statement—It is recommended that the HMO properly report amounts withheld under provider contracts as part of Claims Payable in future statutory financial statements, as required by the NAIC *Annual Statement Instructions—HMO*.
5. Page 25 - Disaster Recovery Plan—It is recommended that the board formally acknowledge and document its acceptance of EIW's disaster recovery/contingency plans.

IX. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the HMO is acknowledged.

In addition to the undersigned, the following representative(s) of the Office of the Commissioner of Insurance, state of Wisconsin, participated in the examination:

Name	Title
Danielle C. Rogacki	Insurance Examiner
Randy Milquet	Insurance Examiner—Advanced

Respectfully submitted,

Amy M. Johnson
Examiner-in-Charge

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